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FEDERAL COMMUNICATIONS COMMISSION
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ORIGINAL FILE

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Open Network Architecture Tariffs of Bell Operating Companies	)	CC Docket No. 92-91
	)	

REPLY TO OPPOSITIONS

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November 13, 1992

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SUMMARY

In this Reply, U S WEST Communications, Inc. ("U S WEST") responds to Oppositions directed at its Service Cost Model ("SCM") ONA Direct Case and the Arthur Andersen Review. In evaluating the myriad of documents filed in this tariff proceeding, the Federal Communications Commission ("Commission") must not lose sight of the sole purpose of its investigation -- that is, to determine whether Bell Operating Company ("BOC") ONA tariffs are unjust and unreasonable and in violation of the Communications Act. If the Commission is unable to determine whether specific rates are just and reasonable, it should subject them to further investigation rather than allow a few "outliers" to delay the conclusion of the instant tariff proceeding.

U S WEST has demonstrated in its Direct Case, SCM submissions and this Reply that its cost methodologies and resulting ONA rates are just and reasonable. U S WEST has made no attempt to explain the differences between its ONA rates and the rates of other BOCs. U S WEST cannot defend or explain the rates of other parties and has no legal obligation to do so. U S WEST has fully complied with all relevant Commission rules in developing its ONA rates. As such, U S WEST requests that the Commission find U S WEST's ONA rates to be just and reasonable and terminate its investigation.

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REPLY TO OPPOSITIONS

U S WEST Communications, Inc. ("U S WEST"),[1] through counsel and pursuant to the Federal Communications Commission's ("Commission") Order issued on August 14, 1992,[2] hereby files its Reply to Oppositions to U S WEST's Direct Case on its Open Network Architecture ("ONA") tariff, which was filed on May 18, 1992.[3]

I. INTRODUCTION

In its Designation Order, the Commission designated a number of issues associated with Bell Operating Company ("BOC")

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[1] U S WEST is a common carrier provider of exchange access and exchange telecommunications services.

[2] See Commission Requirements for Cost Support Material to be Filed with Open Network Architecture Access Tariffs, 7 FCC Rcd. 5307 (1992).

[3] Oppositions were filed on October 16, 1992, by the following parties: Ad Hoc Telecommunications Users Committee ("Ad Hoc"), Allnet Communication Services, Inc. ("Allnet"), American Telephone and Telegraph Company ("AT&T"), General Services Administration ("GSA"), MCI Telecommunications Corporation ("MCI"), Metromedia Communications Corporation ("Metromedia"), Sprint Communications Company LP ("Sprint"), and WilTel, Inc. ("WilTel").

ONA tariffs for investigation.[4] The Commission's primary purpose was to examine the wide disparity between BOC ONA tariffs and to determine if the various rates are reasonable.[5] In a parallel proceeding, the Commission examined the validity of the cost models which the BOCs used in developing their ONA rates.[6]

On May 18, 1992, U S WEST filed its Direct Case in response to Commission inquiries in the Designation Order. U S WEST's Direct Case only addressed the cost model inputs and methodologies which were used in the development of U S WEST's ONA rates. U S WEST did not comment on the ONA rates or cost methodologies of other BOCs. In the cost model proceeding (i.e., SCIS Disclosure Order), parties signing nondisclosure agreements were allowed to examine redacted versions of U S WEST's Switching Cost Model ("SCM"). In this same proceeding, Arthur Andersen was engaged to conduct an independent review of the SCM and Switching

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[4] See Open Network Architecture Tariffs of Bell Operating Companies, Order Designating Issues for Investigation, 7 FCC Rcd. 2604 (1992) ("Designation Order"). See also Public Notice, DA 92-570, rel. May 7, 1992, clarifying the pleading cycle.

[5] U S WEST's ONA tariffs were contained in Transmittal No. 206 and filed with the Commission on November 1, 1991. The Commission suspended Transmittal No. 206 for one day and U S WEST's ONA rates became effective on February 2, 1992, subject to an accounting order. See US West Communications, Inc. Revisions to Tariff F.C.C. No. 1, Open Network Architecture Tariffs, 7 FCC Rcd. 1512, 1513 ¶ 4 (1992).

[6] See Commission Requirements for Cost Support Material To Be Filed With Open Network Architecture Access Tariffs, 7 FCC Rcd. 1526 (1992) ("SCIS Disclosure Order").

Cost Information System ("SCIS") models.[7] As a result, Oppositions were directed at the SCM/SCIS cost models and the Arthur Andersen review in addition to BOC Direct Cases.

Not surprisingly, parties filing oppositions attacked BOC ONA rates, cost methodologies, cost models, overhead loadings, direct costs and Arthur Andersen's review of BOC cost models, among other things. In the face of this barrage of criticism, it is easy to lose sight of the purpose of this tariff investigation. To reiterate -- the sole purpose of this proceeding is to determine whether BOC ONA tariffs are unjust and unreasonable in violation of the Communications Act, not to prescribe costing methodologies for developing rates for ONA services or any other services. Time and again, opponents try to obscure the purpose of this proceeding in their comments by attacking things such as the validity of Arthur Andersen's independent review of the SCM/SCIS cost models and the lack of uniformity in BOC costing methodologies.[8]

The Commission should ignore such diversionary attacks and focus on the issue of whether a given BOC's ONA rates are

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[7]Arthur Andersen's review covered four areas: evaluation of SCIS/SCM methodology; identification of study parameters subject to variation; sensitivity analyses; and validation of SCIS/SCM aggregation methods.

[8]U S WEST would have been quite happy to forego the time and expense of the Arthur Andersen review. Ironically, the scope of this review was largely shaped by the concerns of intervenors and the Commission, not the BOCs. The primary concerns of the BOCs were to ensure that their proprietary cost models were not misappropriated and that confidential vendor information was not revealed.

reasonable or not. If the Commission is unable to determine whether specific BOC rates are just and reasonable, it should subject them to further investigation rather than allow a few "outliers" to delay the conclusion of the instant proceeding.

U S WEST has fully complied with all applicable Commission rules in developing its ONA rates. U S WEST believes that its cost methodologies and resulting ONA rates are just and reasonable. U S WEST has not and will not attempt to explain the differences between its ONA rates and the rates of other BOCs.[9] It is hardly surprising that ONA rates vary among the BOCs given that: the BOCs had different rates for previously-bundled feature groups;[10] used different cost methodologies for calculating direct costs and assigning overheads; and had different levels of projected demand.

In the sections which follow, U S WEST will address several of the issues raised in oppositions to its Direct Case. U S WEST makes no attempt to respond to all the allegations of opponents -- many of these allegations are directed at other BOCs, others are just not relevant to this proceeding. Also, U S WEST will not respond to attacks on the validity of Arthur Andersen's review in these comments. The Commission has

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[9]U S WEST has no lawful obligation to defend the rates of others or to even explain the differences between its rates and those of others.

[10]As of July 1992, BOC prices for the LS1 element of Feature Group B service ranged from 2.411-3.985 cents per minute and the prices for the LS2 element of Feature Group D service ranged from 2.395-3.937 cents per minute.

sufficient information to evaluate Arthur Andersen's work and to determine the weight that it should be accorded in this proceeding.

II. ARGUMENTS THAT BOCs "STRATEGICALLY" PRICED THEIR BSEs ARE WITHOUT MERIT WITH RESPECT TO U S WEST

Opponents claim that the BOCs engaged in "strategic pricing" of BSEs.[11] This is not true with respect to U S WEST's pricing of its BSEs. Strategic pricing implies that a service provider is assigning its costs and establishing prices to advantage itself in those markets where it faces greater competition. While this is a logical and legitimate response to competition which is not unlawful, it is virtually impossible to engage in strategic pricing if a service provider uses a consistent methodology to determine the direct costs of its services and assigns overhead loadings in a uniform manner. This is exactly what U S WEST did in developing its BSE rates.

U S WEST used a common costing methodology for determining the direct costs associated with each of its BSEs. U S WEST then used the same overhead loading factor for all BSE's (i.e., 138%).[12] As such, opponents' claims of strategic pricing have no relevance with respect to U S WEST's pricing of its BSEs.

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[11] See MCI at 3-4, 24; Ad Hoc at 9.

[12] U S WEST provided a detailed explanation of how its overhead loading factor was developed in its Direct Case. See U S WEST Direct Case, filed May 18, 1992, at Appendix D.

III. BOCs ARE NOT REQUIRED TO USE THE SAME COSTING METHODOLOGY TO DEVELOP RATES FOR BSEs OR ANY OTHER NEW SERVICES

A number of opponents attack BOC ONA rates because they were developed using different costing methodologies[13] and some opponents go so far as to advocate that the Commission prescribe a uniform costing methodology.[14] However, Commission rules do not require local exchange carriers ("LEC") to use the same costing methodology -- only that a given LEC use the same costing methodology for all related services. The Commission made this very clear in its Part 69/ONA Order in which it ordered the BOCs to file ONA tariffs.

> LECs may develop their own costing methodologies, but they must use the same costing methodology for all related services.[15]

Thus, while opponents' assertion that there is a lack of uniformity in costing methods among the BOCs may be true, it is not a basis for finding BOC ONA rates to be unjust and unreasonable. Even though the Commission might arguably find uniform costing methods to be in the public interest after an appropriate rulemaking, this tariff proceeding is not the proper forum for making such a finding. Furthermore, there is no record

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[13] See Wiltel at 37; Sprint at 2-3; MCI at 3, 18-19.

[14] See Ad Hoc at 10-11; Allnet at 5-6; MCI at 21, 24; Wiltel at 40.

[15] See Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, Policy and Rules Concerning Rates for Dominant Carriers, 6 FCC Rcd. 4524, 4531 ¶ 42 (1991) ("ONA/Part 69 Order").

in this proceeding to support such a finding. As such, opponents' arguments on costing uniformity must be dismissed as irrelevant to the instant tariff proceeding.

IV. U S WEST'S OVERHEAD LOADINGS ARE NOT UNREASONABLE

Opponents either contend or imply that U S WEST's overhead loadings are unreasonable.[16] In calling U S WEST's explanation of its overhead loadings "patently ridiculous," Metromedia asserts that U S WEST has not even attempted to justify its "excessive overhead loadings."[17] This is not true. Metromedia's contention, while steeped in "high-sounding" rhetoric, has no basis in fact. U S WEST will repeat its earlier explanation for Metromedia's benefit.

U S WEST does not deny that its overhead loadings are in excess of 100% of the direct costs of its BSEs. However, this is the same situation which exists with respect to other U S WEST services in the local switching ("LS") category.[18] This is a result of the fact that forward-looking direct costs for local switching investments are significantly less than embedded costs. This should come as no surprise given the fact that per unit costs of switching have been declining.

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[16] See MCI at 23-24; WilTel at 14; Metromedia at 8.

[17] Metromedia at 8.

[18] U S WEST's methodology for assigning overhead loadings to BSEs is in full compliance with the Commission's Part 69/ONA Order and is the same methodology which is employed to assign overhead loadings to U S WEST's other new service offerings.

U S WEST's overhead loading methodology uses the relationship between overhead costs and direct costs for a given Part 69 cost category. This ensures that no service bears a greater share of overhead loadings than the respective Part 69 cost category as a whole. U S WEST fully explained the derivation of its overhead loading factor for its BSEs and for other local switching services in Appendix D of its Direct Case.[19] U S WEST has assigned overhead loadings in a consistent manner. The fact that overhead loadings are high in relation to direct costs is not a basis for finding these loadings to be unreasonable. The Commission has not found U S WEST's overhead loadings methodology to be unreasonable in the past and should not do so now.

V. SCM REDACTIONS ARE NECESSARY TO PROTECT PROPRIETARY VENDOR INFORMATION AND U S WEST'S TRADE SECRETS

Several petitioners raised objections to the second redaction ("Redaction II") of U S WEST's SCM in a further attempt to discredit the Common Carrier Bureau's ("Bureau") disclosure process.[20] Redaction II was performed at the request of the Bureau staff to preserve the confidentiality of the SCM and the vendor data contained therein, while simultaneously enabling participants in the ONA tariff proceedings appropriate access to the cost data. In effect, intervenors were allowed access to the

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[19] See n.12 supra.

[20] See Ad Hoc at 4-7; Metromedia at 9-13; Sprint at 4-7; Allnet at 8-9; Wiltel at 18-20; and MCI at 32-34.

SCM documentation and software, minus the switching vendors' proprietary data and algorithms that represent the intellectual property and trade secrets of U S WEST. In compliance with the Bureau's directions, U S WEST invited all parties signing nondisclosure agreements and notices of compliance to review the SCM's Redaction II.[21]

Several petitioners argued that the SCM's algorithms should be disclosed. The algorithms are mathematical equations that form the "brain" of the SCM and they cannot be segregated from the embedded proprietary vendor data. Thus, disclosing the algorithms would in essence force U S WEST to reveal its confidential vendor data. As explained time and again in this proceeding, U S WEST is prohibited by contractual agreements from revealing proprietary vendor data without the vendor's concurrence. It is significant to note that the U.S. District Court for the District of Columbia has also determined that the SCM itself is commercial and financial material properly withheld under Exemption 4 of the Freedom of Information Act ("FOIA").[22]

Suffice it to say that to the extent the algorithms are

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[21] See Letter from Anna Lim, Counsel, Federal Relations, USWC, to Cheryl Tritt, Chief, Common Carrier Bureau, dated July 31, 1992. AT&T, US Sprint, Metromedia and WilTel accepted the invitation and reviewed Redaction II during the period August 19-26 in Washington, D.C. MCI, Allnet and Ad Hoc declined to review Redaction II. USWC finds it curious that these three parties will now complain about the adequacy as well as the review process of SCM Redaction II.

[22] See Memorandum Opinion of Charles R. Richey, United States District Judge, Civil Action No. 92-1350 (CRR), dated Aug. 31, 1992.

an important part of the model, they are useful only in reaching a determination as to the reasonableness or soundness of the model itself. That evaluation has been exhaustively performed by Arthur Andersen which rendered an opinion on the reasonableness of the model and its algorithms. Inasmuch as the Andersen opinion has been rendered, release of the SCM algorithms themselves would serve no useful purpose, but would subject U S WEST and the switch vendors to unacceptable competitive risk.[23]

As a result of a series of discussions and meetings with the Bureau staff, switch vendors and intervening parties on Redaction II, U S WEST eliminated all competitively sensitive switch vendor information from the SCM. It is significant to note that the switch vendors themselves -- AT&T and Northern Telecom -- made the determination as to whether or not to disclose pricing specifics or switch architecture information that could be used directly or indirectly against them. U S WEST's SCM Redactions were performed to satisfy these vendor concerns.

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[23]Allnet questions the objectivity of Arthur Andersen, implying that since they are paid by the BOCs, they must be biased. This claim is simply outlandish. Allnet has not provided one scintilla of proof that Arthur Andersen has not performed its duty in an impartial and professional manner. The Commission should reject Allnet's red-herring claim forthwith. <u>See</u> Allnet at 1-2.

VI. THE ARTHUR ANDERSEN REPORT REPRESENTS THE PRODUCT OF AN INDEPENDENT REVIEW WHICH WAS LARGELY SHAPED BY THE CONCERNS OF THE BUREAU AND PETITIONERS

At the request of the Bureau, U S WEST and the other BOCs hired Arthur Andersen to conduct an independent review of their SCIS/SCM models in conjuction with the ONA tariff proceeding. On March 5, 1992, Arthur Andersen filed its proposed work plan with the Commission on the public record. At the request of the Bureau staff, Arthur Andersen conducted a workshop for petitioners on May 13, 1992 during which it described the scope of work to be performed and the analyses to be conducted. Petitioners were allowed to submit comments on the Andersen review process pursuant to a May 15, 1992 letter from the Bureau Chief. In response to petitioners comments, the scope of the independent review was broadened. The July 1992 Arthur Andersen Independent Review of SCIS/SCM Report, describes the process by which input was solicited from interested parties including switch vendors, intervenors, and the Commission staff. Accordingly, it is ludicrous for the petitioners to now complain that the Andersen Report is nothing but a BOC-sponsored report.

The Andersen Report examines the costing principles and designs of the cost models as they pertain to ONA BSE costs, and validates that the SCIS/SCM meet these principles. The report identifies the input values, model parameters, and other factors used by U S WEST and others in their cost models in order to develop BSE costs, and to determine whether the resulting cost information is consistent with the costing principles and design objectives. The Andersen Report also examines the reasonableness of methods used by the BOCs to aggregate SCIS/SCM cost results to compute BSE costs and to identify the differences among the BOCs in these methods.[24]

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[24]Contrary to some of the petitioner's arguments, Arthur Andersen was not asked to pass judgement on the validity of the costing principles themselves. Rather, Andersen was to evaluate whether BSE cost data was consistent with the costing principles that the BOCs incorporated in their models, and whether the models were likely to produce reasonable results.

VII. COMPETITIVELY SENSITIVE INFORMATION PURSUANT TO PROTECTIVE AGREEMENTS

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VIII. CONCLUSION

As the foregoing and U S WEST's Direct Case demonstrate, U S WEST fully complied with all Commission rules in developing its ONA tariff. As such, the Commission should find that U S WEST's rates for its BSEs are just and reasonable and terminate its investigation.

Respectfully submitted,

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November 13, 1992

CERTIFICATE OF SERVICE

I, Kelseau Powe, Jr., do hereby certify on this 13th day of November, 1992, that I have caused a copy of the foregoing **REPLY TO OPPOSITIONS** to be mailed via first class mail, postage prepaid, to the persons named on the attached service list.

Kelseau Powe, Jr.

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